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UNCLAS SECTION 01 OF 05 TOKYO 003104

SENSITIVE
SIPDIS

DEPT FOR EAP - AMBASSADOR HASLACH
DEPT ALSO FOR EAP/J AND EEB/OIA
DEPT PASS USTR FOR CUTLER, BEEMAN, KALLMER
NSC FOR LOI
TREASURY DEPT FOR DAS NOVA DALY, AND IA/CARNES
JUSTICE FOR ANTITRUST DIVISION - CHEMTOB
USDOC FOR 4410/ITA/MAC/OJ
GENEVA FOR USTR

E.O. 12985: N/A

TAGS: [EINV](#) [ECON](#) [PREL](#) [OECD](#) [JA](#)

SUBJECT: U.S.-JAPAN INVESTMENT WORKING GROUP CALLS FOR POSITIVE
TRADE AND INVESTMENT AGENDA

Sensitive but Unclassified - Not for the Internet

11. (SBU) Summary: The eighth round of talks under the U.S.-Japan Bilateral Investment Working Group (IWG) took place October 29 in Tokyo co-chaired by U.S. Ambassador to APEC Patricia Haslach and Ministry of Economy, Trade and Industry (METI) Deputy Director General Makoto Shiota. The two sides exchanged views on the current turmoil in global financial markets and its impact on cross-border investment flows, and agreed on the need to cooperate to fight trade and investment protectionism. The IWG continued its examination of the each country's FDI review processes, including the U.S. FINSA law and Japan's Foreign Trade Control Act. The GOJ provided a clarification of the term "risk to public order", the legal provision on which it blocked a proposed foreign investment in J-Power Corporation in May 2008. METI presented a non-paper with recommendations to the U.S. on implementation of enhanced marine cargo security reporting requirements. Both sides exchanged views on the status of bilateral investment negotiations with third countries. At the conclusion of the talks, the co-chairs issued a joint press release reaffirming both countries' commitment to maintaining open investment regimes. End Summary.

Re-emphasizing the Importance of Open FDI Regimes

12. (SBU) Shiota opened the session by noting that over the eight years of the bilateral Investment Initiative Japan's stock of foreign direct investment (FDI) has more than doubled from 6.6 trillion yen to more than 16 trillion yen today. Nevertheless, Japan is concerned the global economic slowdown resulting from recent turmoil in world financial markets could reduce cross-border investment flows and jeopardize Japan's achievement of its target of FDI stock equivalent to five percent of GDP by FY 2010. Ambassador Haslach agreed that because of the market turmoil this is an excellent time to acknowledge once again the important contribution of cross-border investment to economic prosperity in both countries.

¶3. (SBU) Ambassador Haslach described the decisive actions the U.S. Government is taking to stabilize the U.S. banking system, maintain liquidity in credit markets, and restore market confidence as quickly as possible. The G-20 meeting set for November 15 would be another opportunity to strengthen cooperation on policies toward national financial market. However, the best way to restore confidence, Haslach noted, was to maintain a robust trade and investment agenda.

¶4. (SBU) Shiota agreed the current global financial turmoil requires a global response and emphasized the GOJ continues to seek foreign direct investment, in particular FDI from the U.S., which accounts for 40 percent of all Japanese inward FDI and is "indispensable" for the promotion of on-going economic and technological development in Japan. Noriyuki Shikata, Director, Second North Americas Division, Ministry of Foreign Affairs (MOFA), added both countries need to cooperate to fight against trade and investment protectionism.

¶5. (SBU) Ambassador Haslach proposed -- and DDG Shiota immediately agreed -- the two governments issue a joint press release following the IWG meeting reaffirming commitment of both countries to maintaining an open investment regime. The text of the joint statement is contained in paragraphs 25-29.

Implementation of Investment Expert Report

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¶6. (SBU) Hiroaki Hara, Director of Foreign Investment Promotion, Cabinet Office, briefed the Working Group on the implementation of the May 2008 recommendations of the GOJ ad-hoc Investment Experts Committee report. The Cabinet incorporated the recommendations into the GOJ's annual report on the government's Basic Economic and Fiscal policies issued in June 2008.

¶7. (SBU) METI had begun implementing the experts committee's recommendation to identify and clarify Japan's M&A rules with the July 2008 report of METI's Corporate Value Study Group. In the meantime, the Cabinet Office will review the grounds and scope for discriminating between domestic and foreign investors on security grounds. The Cabinet Office plans to hold hearings on this subject in the coming weeks with an aim of issuing a report by the end of ¶2008.

¶8. (SBU) Hara added internal discussion of the other recommendations continues. The Cabinet and ruling coalition will need to address the most controversial recommendation -- reducing Japan's 40 percent corporate tax rate -- within the context of other changes to Japan's tax system, including Japan's consumption tax rate. However, Hara anticipated the ruling party will discuss corporate tax rates during the review of possible FY-2009 tax changes, a process which will be completed by December 2008.

Security Reviews Should Not Unreasonably Hinder FDI

¶9. (SBU) Michael Carr, Senior Policy Analyst from the U.S. Treasury Department, told the working group that implementation of the U.S. Foreign Investment and National Security Act of 2007 (FINSA) is in its final stage. Issuance of final rules is imminent. At each stage of implementation, the USG's key objective has been to reinforce its long-standing commitment to an open investment regime. The Treasury-led CFIUS committee, which reviews selected FDI transactions, had hoped to have completed the final rule already, but the need to review a large volume of public comments has necessitated a delay. The comments have been generally positive, Carr noted, but many emphasized the importance of greater transparency in the CFIUS review process.

¶10. (SBU) Carr also discussed the concept of "control", which governs whether CFIUS has authority to review a potential transaction. CFIUS' definition of "control" is based on whether the

new owners would be in a position to direct corporate decisions. The concept of control is embedded in the law and, Carr noted, is a "functional" test and not based on a simple numerical level of shareholding.

¶11. (SBU) Treasury also plans to publish guidelines and a narrative discussion of the national security criteria set out in the FINSA to provide greater clarity to the process. The overall aim of the CFIUS review is to resolve concerns to the extent possible and allow transactions to proceed, not to block transactions.

METI Clarifies Meaning of "Risk to Public Order"

¶12. (SBU) Yasuhito Nii, Director of METI's Trade and Investment Facilitation Division, briefed on recent GOJ reviews under the Foreign Exchange and Trade Act (FEFTA), specifically addressing U.S. concern about the definition of "risk to public order", which was the rationale used to block a proposed foreign investment in electricity wholesaler J-Power Corporation in May 2008.

¶13. (SBU) Nii explained "public order" is one of three criteria for

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investment restriction contained in the OECD Code on Liberalization of Capital Movements. The GOJ decision to block the investment in J-Power, Nii insisted, was not taken easily or lightly. But the GOJ decided that Japan had an overriding public interest in maintaining the current level of operation in certain critical public infrastructure, in this case, J-Power's power grids and the planned Ohma Nuclear power plant. Nii added such a determination was made on a case-by-case basis and the decision on the J-Power case does not imply the GOJ seeks to wall off whole industrial sectors from foreign investment.

¶14. (SBU) In response to a specific U.S. question, Nii confirmed the risk to public order determination in the J-Power case was intended to ensure that Japan maintained control of certain critical technological infrastructure, and was not aimed at protecting that technology from falling into foreign hands. In other words, the GOJ did not determine the proposed foreign investment was threat to Japan's national security.

Mitigation Strategies

¶15. (SBU) Carr briefly explained the rationale behind CFIUS use of mitigation strategies in certain cases. CFIUS views such mitigation agreements as a "proportionality tool", which should be used in cases where other laws are inadequate or inappropriate to achieve the desired outcome. The number of mitigation agreements CFIUS has entered into is low relative to the number of cases handled, has declined in recent years. METI's Nii noted that Japan does not have a provision for mitigation strategies in the FEFTA. In large part, he said, this reflected the fact the Japanese law, in contrast to the U.S. or UK, establishes a pre-notification system rather than an ex-post facto system. Nii then asked how the U.S. enforces such agreements and what legal authority the USG has in cases where the agreement is breached. Carr noted that CFIUS has authority to take action in cases of breaches of mitigation agreements, and would look to existing law to enforce such agreements.

¶16. (SBU) In response to a question, Nii added the Cabinet Office review of the FEFTA system, as called for in the Expert Committee report, will be focused on how to improve the transparency of the system. The GOJ has no plans to amend the list of sectors subject to the notification and pre-approval requirement.

FEFTA Impact on Mutual Funds

¶17. (SBU) The USG submitted a paper outlining the negative impact of the increasing compliance burden of FEFTA on passive investors such as mutual funds. The U.S. noted this appears to be a case of unintended consequences of investment regulations that potentially inhibit portfolio investment Japan says it wants to attract to make

Tokyo an international financial center. Ambassador Haslach indicated the U.S. also plans to make specific recommendations in this area in the Financial Services Working Group of the Regulatory Reform Initiative.

Cargo Security

¶18. (SBU) Yasushi Akahoshi, Director of METI's Americas Division, presented a non-paper outlining specific recommendations on implementation of U.S. Customs and Border Protection (CPB) proposal to strengthen cargo security reporting requirements (the "10 plus 2" program.) Embassy faxed a copy of the non-paper to EAP/J.

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¶19. (SBU) The non-paper urges CPB to conduct a pilot project to test the desirability and impact of the new rules and to postpone final implementation of the rule to allow CPB to evaluate the feasibility and impact of the new rule. The GOJ also urges the USG to exempt companies "certified and validated" as Customs-Trade Partnership against Terrorism (C-TPAT) participants from the importer security filing requirement.

¶20. (SBU) Ambassador Haslach assured the GOJ that "the U.S. hears your concern" about 10 plus 2. She promised to pass the non-paper to the Embassy CPB attach. She added that release of a final rule in this area is expected soon, but the exact date is uncertain. She also said the USG expects there will be a phased period of implementation, and urged the GOJ to present its non-paper as well at the next digital video conference of the Study Group on Secure and Efficient Trade planned for early November.

Bilateral Investment Treaties

¶21. (SBU) Continuing a discussion begun in previous working group meetings, the two sides briefed on recent developments in negotiations of bilateral investment treaties (BIT) with third countries. Noriyuki Mita, Director of METI's Economic Partnership Agreement Division, reviewed the history of Japan's BIT strategy. Since early 2007, Japan has actively pursued BITs with individual trading partners not currently ready to enter into negotiations on full-scale Economic Partnership Agreements. Japan will seek to expand such agreements, especially with countries in the Middle East, Africa, and Central Asia, where there is increased Japanese investment in resources sectors.

¶22. (SBU) Ambassador Haslach explained the United States is actively pursuing BITs with numerous economies. This year, the U.S. formally launched BIT negotiations with China, India, and Vietnam and held BIT-related discussions with Brazil, Gabon, Georgia, Ghana, Indonesia, Mauritius, and Pakistan. The U.S. and Japan, she emphasized, should cooperate to promote a global web of high-standard international investment agreements. Such agreements could set positive precedents for future investment agreement negotiations worldwide. The July 2008 G8 Declaration underscored the importance of these objectives.

¶23. (SBU) Ambassador Haslach explained the status of the U.S. ongoing BIT negotiations with China, which were launched at the fourth U.S.-China Strategic Economic Dialogue. Two negotiating rounds have taken place, and based on the content of the talks to date, there appears to be significant common ground with China on core investor protections -- such as those on expropriation and "fair and equitable treatment" -- as well as on investor-State arbitration. However, there are fundamental differences in the area of national treatment and exceptions to the national treatment obligations on a negative list basis. Mita reported Japan's negotiations on a trilateral Japan-China-Republic of Korea BIT were meeting similar obstacles.

Looking Ahead

¶24. (SBU) Both sides agreed to hold the next IWG meeting in the

first quarter of 2009. Before then, the two sides will consult internally as well as with each other on possible new items to add to the working group agenda that might spur expanded cross-border FDI.

Text of Joint Press Statement

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125. (U) Joint Press Statement by the Co-Chairpersons of Japan-United States Bilateral Investment Working Group

126. (U) The Japan-United States Bilateral Investment Working Group was held on October 29, 2008 in Tokyo. The Working Group was co-chaired by Mr. Makoto Shiota, Deputy Director-General of Trade Policy Bureau, METI (Ministry of Economy, Trade and Industry) and Ambassador Patricia Haslach of the U.S. Department of State.

127. (U) The two chairs expressed the common view on the importance of continuing to promote foreign direct investment, taking careful note of the current economic downturn caused by the recent financial market turmoil. A positive trade and investment agenda will contribute to rapid return to prosperity and economic growth.

128. (U) In today's meeting, both sides exchanged and updated information and views on:

-- Our respective investment climates, including the recommendations of the Expert Committee on FDI Promotion on the Japanese side;

-- Cargo Security issues, including "10 plus 2" rules, and 100% scanning;

-- Security Related Investment Reviews, including updates on the U.S. FINSA (Foreign Investment and National Security Act) and implementation of Japan's FEFTA (Foreign Exchange and Foreign Trade Act);

-- Negotiations toward a U.S.-China Bilateral Investment Agreement and other Bilateral Investment Treaties as well as Japan's global strategy on negotiating Bilateral Investment Treaties.

129. (U) The Investment Working Group is one aspect of the Japan-U.S. Investment Initiative, which is a key component of the cooperative framework of the Japan-U.S. Economic Partnership for Growth. This framework was launched by then Prime Minister Junichiro Koizumi and President George W. Bush in 2001. The Japan-U.S. Investment Initiative is aimed at promoting bilateral direct investment between the two countries, by holding wide-ranging discussions related to investment climate and investment rules and regulations. (End text)

130. (U) Ambassador Haslach cleared this cable subsequent to her departure from Tokyo.

SCHIEFFER